No. 85-521

In The

Supreme Court of the United States

October Term, 1985

OTIS R. BOWEN, SECRETARY OF HEALTH AND HUMAN SERVICES, ET AL.,

Appellants,

v.

PUBLIC AGENCIES OPPOSED TO SOCIAL SECURITY ENTRAPMENT, ET AL.,

Appellees.

UNITED STATES OF AMERICA, ET AL.,

Appellants,

v.

STATE OF CALIFORNIA,

Appellee.

On appeal from the United States District Court for the Eastern District of California

BRIEF ON THE MERITS FOR APPELLEES PUBLIC AGENCIES OPPOSED TO SOCIAL SECURITY ENTRAPMENT, ET AL.

Ernest F. Schulzke
General Counsel
Blanning & Baker
Associates, Inc.
660 J Street, Suite 443
Sacramento, CA 95814
(916) 441-2222
Attorney for Appellees

COCKLE LAW BRIEF PRINTING CO. (800) [illegible]

QUESTIONS PRESENTED

1. Whether the fundamental principle that Congress is without power unilaterally to repudiate contractual obligations of the United States may be ignored by Congress in enacting legislation which unilaterally abrogates and/or repudiates a provision of a written contract entered into by the United States as a party thereto.

2. Whether the unilateral abrogation and/or repudiation by Congress of the agreed upon right to withdraw from the Social Security system, which right is one provision of a larger written contract between the United States and the State of California and its political subdivisions, effected a "taking" of property within the meaning of the Fifth Amendment.

PARTIES TO THE PROCEEDING

The list of parties plaintiff in Appellants' Brief on the Merits is incomplete. Accordingly, a complete list hereby is submitted as follows:

Public Agencies Opposed to Social Security Entrapment (POSSE)

General Law Cities:

Alturas
Arcata
Lincoln
San Clemente
San Anselmo

Charter City:

Redondo Beach

Special Districts:

Aromas Tri-County Fire Protection District
Bear Mountain Recreation and Park District
Big Bear Municipal Water District
Delano Mosquito Abatement District
Humboldt Community Services District
Marin Municipal Water District
North Bakersfield Recreation and Park District
Paradise Irrigation District
Paradise Recreation and Park District
Pico Water District
Placentia Library District
Rancho Simi Recreation and Park District
Salispuedes Fire Protection District
Yorba Linda Library District

Individual Plaintiffs:

Katherine T. Citizen
Margie Hunt
William Rasmussen

(See Amendment to Amended Complaint, District Court Record Docket Nr. 28 dated January 4, 1984.)

TABLE OF CONTENTS

TABLE OF CONTENTS—Continued

TABLE OF AUTHORITIES

TABLE OF AUTHORITIES—Continued

CONSTITUTION AND STATUTES:

TABLE OF AUTHORITIES—Continued

TABLE OF AUTHORITIES—Continued

No. 85-521

In The
Supreme Court of the United States
October Term, 1985

OTIS R. BOWEN, SECRETARY OF HEALTH AND HUMAN SERVICES, ET AL.,
Appellants,
v.
PUBLIC AGENCIES OPPOSED TO SOCIAL SECURITY ENTRAPMENT, ET AL.,
Appellees.

UNITED STATES OF AMERICA, ET AL.,
Appellants,
v.
STATE OF CALIFORNIA,
Appellee.

On appeal from the United States District Court for the Eastern District of California

BRIEF ON THE MERITS FOR APPELLEES PUBLIC AGENCIES OPPOSED TO SOCIAL SECURITY ENTRAPMENT, ET AL.

STATEMENT

Of the twenty-four Appellees herein (hereafter "Public Agencies"), twenty are public agencies within the State of California. Six are cities while fourteen are special dis-

tricts organized pursuant to the laws of California. Many if not most are participants in California's Public Employees' Retirement System ("PERS").

For a number of years prior to the creation of the Social Security System ("System") in 1935, California had provided a retirement system both for its own employees and those of its political subdivisions. (See generally, California Government Code Section 20002 *et seq.*) The Social Security Act ("Act") was passed to meet a need. In California that need already was being met for public agencies by PERS. It therefore made sense that the Act as originally contemplated generally excluded state employees except those who were not already protected by a retirement system. Protection was the Act's purpose. And protection was necessary only for those who did not already have coverage.

A further consideration in excluding such employees from the System was "questions as to the constitutionality of any general levy of the employer tax on States and localities." (For a discussion of the evolution of the involvement of State and local governments in the System please refer to *Brief of Council of State Governments, et al., as Amici Curiae in Support of Appellees,* Statement, hereinafter cited as "*Amici Br.*")

So it was that when the 1950 Amendments were enacted, the relevant section was entitled "*Voluntary* Agreements for Coverage of State and Local Employees." (1950 Amendments Sec. 106 adding Sec. 218 to the 1935 Act; 42 U.S.C. 418, referred to herein as Section 418.) (Emphasis added.) Underscoring the voluntary nature of state and

local participation is the directive of Section 418 that the "Administrator shall, *at the request of any State,* enter into an agreement. . . ." (Emphasis added.)

Further underscoring the voluntary nature of the coverage 42 U.S.C. 418(g) provided that a state was at liberty to terminate the coverage of its own employees or those of its political subdivisions "at the instigation of the State or at the request of the political subdivision itself." Subcommittee on Social Security of the House Committee on Ways and Means. 97th Cong., 2d Sess., WCMP: 97-34, *Termination of Social Security Coverage for Employees of State and Local Government and Nonprofit Groups* 20 (Comm. Print 1982). The right to terminate was seen by Congress as a "necessary corollary" to the voluntary nature of state and local participation. (*Id.,* at 3).

It was against that background that, effective January 1, 1951, the United States executed such a written Agreement ("Agreement") with the State of California ("State"). The Agreement provided for the extension of Social Security coverage to the State and to local "coverage groups." It was signed on behalf of the State by California's Director of Finance and on behalf of the United States by the Acting Federal Security Administrator. (J.A. 29-33).

The Agreement provided that the State could upon fulfillment of certain prerequisites, withdraw its own employees or those of any coverage group upon two years' written notice to the Secretary. (See J.A. 31 par. (F)—Termination by the State).

To implement the Agreement with the United States the State enacted enabling legislation authorizing the

State to enter into individual agreements with its political subdivisions at their request. (California Government Code Section 22000 *et seq.* Deering's 1973 and 1986 Supp.). The Public Agency Cities and Special Districts are among those entities which chose to participate in the System. Their agreements with the State were binding.

While all of the agreements between the Public Agencies and the State are not identical they contain essentially the same terms. Virtually all contain words such as these found in the agreement between the City of Redondo Beach and the State:

> "8. After the filing of this application and agreement, its acceptance and execution by the State shall constitute it a *binding agreement* between the Applicant and the State of California with respect to the matters herein set forth." (Emphasis added.)

(Page 302 of *Exhibit A to Declaration of Richard T. Baker* in Support of Motion for Summary Judgment dated October 17, 1983, *District Court Docket Entry 11*, hereinafter "Docket Entry 11").

In choosing to enter the System the Public Agencies were well aware of the termination option authorized by Section 418(g) and contained in the Agreement. They further noted that the State's enabling legislation also provided that option. (California Govt. Code Sec. 22310). Each of their individual agreements with the State contained a provision incorporating that option.[1] In fact, the

---

[1] The termination provisions are not uniform. While all incorporate the requirements of Section 418(g), approximately half of the agreements executed by Appellee Public Agencies contain the additional requirement that the right of the Public Agen-

(Continued on following page)

option to terminate was a "substantial factor" in the decision by the Public Agencies to enter the System. (See *Affidavit of Richard J. Ramirez,* J.A. 72, par. 13, and *Affidavit of Richard T. Baker* in Support of Motion for Summary Judgment or Partial Summary Judgment 3, par. 6, attached to Plaintiff's Notice and Motion, *District Court Docket Entry 10* dated 10/17/83 hereafter "Docket Entry 10, Baker.") They entered the System "with the understanding and assurance that *if the circumstances suggested it,* the City [of Lincoln] would be able to terminate its social security coverage." (*Ibid.* Ramirez.) (Emphasis added.) In choosing to participate they relied on that assurance.

The Public Agencies became enrolled in the System when the State and the United States modified the federal-state Agreement to include them as a part thereof. (42 U.S.C., 418(c) (4); see also J.A. 31 par. (E) Modification.)[2] They were required by the State's enabling legis-

---

(Continued from previous page)

cy to terminate is contingent upon approval by "a majority vote of its active covered employees." (See e.g., Application and Agreement of City of Alturas, Docket Entry 11 at page 14 paragraph 8). Accordingly, Resolution No. 82-89 of said City, Requesting termination of Social Security, memorialized the vote of a majority of said employees approving termination. (*Ibid.* at 7).

[2] Each such modification contained terms essentially the same as the following provision of Modification No. 4 to California State Social Security Agreement which incorporated the City of Arcata into the Agreement:

> "The Federal Security Administrator and the State of California acting through its representative designated to administer its responsibilities under the Agreement of March

(Continued on following page)

lation and by their agreements, to make certain "contributions" to the State as payment for their participation. (California Government Code Section 22551-53). In return for those contributions they received the benefits afforded by the System, together with the assurance that if circumstances warranted, they could withdraw therefrom.

In recent years local governments such as the Public Agencies have been faced with increasing financial problems. Coincidental with these problems came the rapid acceleration of increases in Social Security contributions. These factors combined to cause the Public Agencies to reevaluate their participation in Social Security. (See. Docket Entry 10, Baker, *supra,* pages 3 through 13 and J.A. 64-73). The decision was made by an increasing number of Agencies that "circumstances suggested" that they exercise their bargained for option to terminate that coverage.

"The requests for termination were submitted for several reasons. Prominent among these was the determination by said public entities that the money which they now spend for Social Security coverage could be more effectively used to provide services to taxpayers, and/or to provide benefit programs for their employees." (*Id.* Docket Entry 10, Baker).

(Continued from previous page)

9, 1951, hereby accept as additional coverage groups under said agreement *and acknowledge the full applicability of the original agreement to . . . .*"

(Docket Entry 11, Page 4. Said Docket Entry 11 contains documents relating to the entry and termination of sixteen of the twenty entities which are POSSE Appellees herein.) (Emphasis added.)

Notwithstanding the foregoing, in April 1983 Congress enacted Public Law No. 98-21, Section 103(a) and (b), amending 42 United States Code Section 418(g), to provide that "[n]o agreement under this section may be terminated, either in its entirety or with respect to any coverage group, on or after April 20, 1983." This amendment, which was enacted thirty-two years after the Agreement between the United States and the State of California was entered into, prevented any state from withdrawing coverage for any of its employees, or those of its political subdivisions, even if a termination notice had been filed and was pending at the time Public Law No. 98-21, Section 103(a) and (b) was enacted.

Through April 1983, the State, which had had its Agreement with the Secretary since 1951, had filed termination notices on behalf of approximately 200 of its political subdivisions. However, Public Law No. 98-21 prevented the terminations from taking place in due course.

The effect upon local governments of the repudiation of the option to terminate ranges from substantial to devastating. For example, the City of Alturas reported that foreclosure of the termination option "could lead to elimination of current services." The City of Arcata reported that it "would result in a cutback in maintenance of infrastructure and buildings." Big Bear Municipal Water District reported that "future increases in social security costs would cause cutbacks in community services." (*Id.* Docket Entry 10, Baker, 4 through 10; see also, Affidavits of Alice Harris and Richard Ramirez, J.A. 64-72).

It was in response to this repudiation of the agreed upon termination provision of the 1951 Agreement that

the Public Agencies filed suit in the United States District Court for the Eastern District of California against the United States and the State of California. They sought a declaration that the said amendment violated the Fifth and Tenth Amendments to the United States Constitution, claiming *inter alia*, that their property had been taken without just compensation. They further sought injunctive relief and specific performance of a contractual obligation of the United States to allow the State and the Public Agencies to terminate. It is that right to terminate which constitutes the property right taken by Appellants. (See J.A. pages 7 and 8). Subsequently the State of California also filed suit against the United States. The suits were consolidated by the district court and are consolidated before this Court.

The district court granted summary judgment to the Public Agencies and the State of California. The basis for that judgment is fairly summarized in U.S. Br. at pages 9 through 11.

———o———

SUMMARY OF THE ARGUMENT

1. This case is about the unilateral repudiation by Congress of a substantial provision of a written Agreement to which the United States was a party. The plethora of cases cited by Appellants (hereinafter "the Secretary") tend to obscure that fact. This case is not about contracts between private parties, or between states and private parties, or between states and other governmental entities. It concerns only contractual obligations agreed to and executed by the United States.

2. The Agreement executed pursuant to 42 U.S.C. 418 constitutes a binding contract between the United States on the one hand, and the State of California and the Public Agencies on the other. It has all of the indicia of a contract, including consideration by both parties. "Under any definition of contract, this is a contract." (Dist. Ct. Opinion, J.S. 30a). The Public Agencies became parties to the Agreement through "Modifications" executed by the Secretary and the State. Through this mechanism they were incorporated into the Agreement. Since the Agreement was made for their benefit, they at least were third-party beneficiaries.

Built into the enabling statute and the Agreement is considerable flexibility to allow the parties to adjust to changing conditions. The Congress may change the enabling statute and the Secretary may change the regulations. But Congress intended that the Public Agencies also should be accorded some flexibility. They were given the option to terminate. That *quid pro quo* was a part of the bargain.

The Agreement was entered into voluntarily. California and the Public Agencies *chose* to enroll in the System on specified terms and conditions. One of those conditions was that if circumstances dictated, the State or any Public Agency could withdraw upon two years' written notice. That condition was an integral part of the Agreement and one of the "motivating causes" of Public Agencies' decision to enter the System.

3. The United States is as much bound by its contractual promises as is an individual. *Sinking Fund Cases,*

99 U.S. 700 (1879); *Perry v. United States*, 294 U.S. 330, 352 (1935). Such contracts are to be interpreted according to the law which applies to contracts between private individuals. *Perry, supra.*

The Secretary has advanced an array of conclusions rather than relevant legal arguments and precedents to support his thesis that the United States did not enter into a contract and if it did, it is not bound thereby. None of these can withstand close scrutiny. The conclusion is inescapable that the United States entered into a binding contract with Appellees.

The binding nature of the contract is not altered by a general statutory reservation of power to alter or amend the *statute*. Such a provision does not empower Congress to amend the *contract*. Rather, it is the laws which subsist at the time and place of making the contract which control the contract's operation. Further, to hold that the United States is bound by its contractual obligations does not derogate from its sovereignty. Instead, "the right to make binding obligations is a competence attaching to sovereignty." *Perry v. United States*, 294 U.S. 330, 353 (1935). The United States did not by the 1951 Agreement diminish its sovereign power to legislate regarding Social Security coverage so long as it does so consistent with the Constitution. Neither convenience nor the lessening of expenditures nor the raising of revenues are valid justifications for the Congress to repudiate its contractual obligations.

4. In revoking the termination option Congress breached a substantial provision of the contract. In choosing to enter the System, the Public Agencies relied on

that option. The ability to leave the System if the cost thereof became prohibitive or if continuation became burdensome was a significant enticement to enroll. Further, it was the *quid pro quo* for the flexibility given the Congress and the Secretary to change the statutes and the regulations.

In filing notices of termination Public Agencies acted responsibly after due deliberation and discussion with their employees. It was determined that it was by terminating Social Security that they best could serve their employees and their constituents. To have done otherwise under those circumstances would have been less than responsible.

5. In repudiating the termination option the United States violated both federal common law of contract and the Just Compensation and Due Process Clauses of the Fifth Amendment. Public Agencies have "rights against the United States arising out of a contract with it" either on their own account or as third-party beneficiaries. They were deprived of a valuable contractual right. That right to terminate the Agreement is worth substantial sums to the Public Agencies and is essential to their ability to provide essential services.

6. The United States has repudiated its own contractual obligation. It therefore should be subject to a "heightened standard of review," which should at least be as rigorous as that used in *United States Trust Co. v. New Jersey*, 431 U.S. 1 (1977). It is not enough to show that the impairment is for a public purpose. It also must be "reasonable and necessary" to accomplish that purpose. In enacting the 1983 Amendments Congress sought to mitigate financial losses to the Social Security System result-

ing from termination of coverage by State and local employees. The 1983 Amendments and the legislative history thereof contain numerous examples of other feasible approaches short of the repudiation of contractual obligations of the United States. It follows that the impairment was not "necessary" and was an unconstitutional taking of property.

—o—

ARGUMENT

INTRODUCTION

In maintaining that the United States unilaterally may repudiate its contractual obligations the Secretary attacks a basic principle of American jurisprudence. Simply stated that principle, which is essential to the integrity of our Government, is that the United States is bound by contractual obligations to which it has agreed and which have duly been executed on its behalf.[3] Ramifications of the denial, the circumvention or the evisceration of that principle in cases such as this would be immense. The

[3] The existence of that principle was acknowledged by this Court in *Perry v. United States*, 294 U.S. 330, 351 fn. 2, wherein it quoted with approval these words of Alexander Hamilton:

> "' . . . *when a government enters into a contract* with an individual, it deposes, as to the matter of the contract, its constitutional authority, and exchanges the character of legislator for that of a moral agent, with the *same rights and obligations as an individual. Its promises may be justly considered as excepted out of its power to legislate, unless in aid of them. It is in theory impossible to reconcile the idea of a promise which obliges, with a power to make a law which can vary the effect of it.*'" (Emphasis added).

element of trust upon which so much of American federalism is based, would be shaken to its foundations.

Beyond the general distrust and frustration which would ensue is the far-reaching economic impact upon the Public Agencies and those similarly situated. That economic impact also has direct ramifications in terms of jobs of the Public Agencies' employees as well as the health, safety and general welfare of the people they serve.[4]

The district court held that, apart from the enabling statute, the Public Agencies have a *contractual* right to withdraw from the System. It held that even if it be assumed *arguendo* that Congress may by statute terminate a *statutory* right to withdraw, it may not abrogate or repudiate its own Agreement executed pursuant to statutory authority. (See, J.S. 31a)

Because this proposition is so clear, simple and undeniable, the Secretary advances an array of conclusions rather than relevant legal authority to support his thesis either that the Agreement is not a contract or that even if it is a contract he is not bound by its terms.

He has generated predictable confusion by liberally infusing into his Brief quotations from and citations to cases dealing with several different types of relationships as

[4] See *Aiffdavits of Alice Harris and Richard Ramirez*, respectively representing the cities of Arcata and Lincoln, California. (J.A. 64-73). For further impacts see *Affidavit of Richard T. Baker, District Court Docket Entry Number 7* dated 8/29/83 pages 3 and 4, and *Affidavit of Richard T. Baker, supra, District Court Docket Entry Number 10* dated 10/17/83, pages 4 through 13. It is clear from the data there presented, which never was challenged or controverted by Appellants, that the financial impact and the impact in terms of the welfare of the people of repudiation of the termination provision is very substantial.

though they virtually are interchangeable. Yet this Court consistently has drawn clear distinctions among them.[5] It bears repeating that this case deals with an express written Agreement to which the United States is a party and to whose terms it freely agreed. This Court consistently has stated that the United States is bound by such contracts. *Perry v. United States,* 294 U.S. 330 (1935); *Lynch v. United States,* 292 U.S. 571 (1934); see also, *National Railroad Passenger Corporation v. Atchison, Topeka & Santa Fe Railway Co.,* No. 83-1492 (Mar. 18, 1985), Slip Opinion 15 and 20 fn. 24.

I

APPELLANTS UNILATERALLY HAVE REPUDIATED THEIR CONTRACTUAL OBLIGATIONS THEREBY DEPRIVING APPELLEES OF THEIR CONTRACTUAL RIGHTS

A. THE UNITED STATES HAS ENTERED INTO A BINDING CONTRACT WITH THE PUBLIC AGENCIES

The Secretary first contends that there is no contract at all. He vaguely refers to a "contractual aspect" which is "unlike normal contractual undertakings." (U.S. Br. pages 11, 12, 18.)

Yet the document which forged his relationship with the State and the Public Agencies is captioned "Agreement." It begins with the words "THIS AGREEMENT

---

[5] The referenced types of relationships are discussed in Public Agencies' Motion to Dismiss or Affirm 6 and 7. In *National Railroad Passenger Corp. v. A.T.&S.F.R.* No. 83-1492, Slip Opinion 14 through 18, this Court gave an illuminating description of the distinction between a "statutory contract" which would "constitute a binding obligation of Congress" and a "regulatory policy" set forth in a statute.

entered into this 9th day of March, 1951 . . . ." It identifies the United States of America as "party of the first part" and the State of California as "party of the second part." It recites the fact that "the parties hereto . . . agree" to certain "terms and conditions."

The Agreement further sets forth mutual covenants, obligations and benefits of both the original parties thereto and employees of political subdivisions of the State.[6] Mutual consideration clearly is evident. Provisions for incorporation of additional parties and/or beneficiaries appear, as do provisions for termination of the Agreement *by either party.* Authorized signatures show that the document was duly executed. (J.A. 29 *et seq.*) The terms are clear and unambiguous.

This Agreement was authorized by Congress in 42 U.S.C. 418. That section provides for the execution of an agreement on behalf of the United States. That a *written* agreement was contemplated is clear. It follows that "the case for an obligation binding upon" the United States also "is clear." *National R. Passenger Corp. v. A.T.&S.F.R., supra,* at 15, citing *Dodge v. Board of Education,* 302 U.S. 74, 78 (1937).

---

[6] In an oblique reference to their Jurisdictional Statement at U.S. Br. 17 fn. 15, the Secretary again asserts that POSSE Plaintiffs were not properly before the district court. The contentions raised at J.S. 9-10 fn. 9 were answered in Public Agencies' Motion to Dismiss or Affirm 15-16. The standing issue was exhaustively briefed and argued in the district court. It further was discussed in detail in the district court's opinion. See J.S. 11a through 22a. In that opinion the district court referred to its discussion of the question of standing in the case of *Sierra Club v. Watt,* 608 F. Supp. 313 (E.D. Cal. April 18, 1985). The foregoing analyses clearly demonstrate that POSSE Plaintiffs were in fact properly before the district court.

Much of what appears in the Agreement expressly was set forth also in Section 418. Clearly set forth at 418(g) was the provision for termination. Its terms were consistent with the termination provisions which were placed into the Agreement. Congress built considerable flexibility into Section 418. For example, Sec. 418(e) provides that the State shall comply with specified types of regulations promulgated by the Secretary. That statutory provision also is reflected in the Agreement. Congress reserved to itself the power to amend the statute. The obvious *quid pro quo* for that grant of discretion to the Secretary and the Congress is the Public Agencies' option to terminate.

It is clear that the enacting Congress intended that there should be flexibility in the administration of the Act. It intended also that State and Local governments should have the flexibility to withdraw if they felt the circumstances warranted it. Without that flexibility the Public Agencies clearly would have struck an "inequitable bargain."

Given that background it is impossible to rationalize the Secretary's bland assertions that "Congress did not intend to create contractual rights" and that "Section 418 agreements have none of the indicia of typical contracts." (U.S. Br. 20 and 22.) To the contrary, this Agreement as well as the enabling statute evidence a clear intent by Congress and the Secretary to enter into a binding contract with the State and the Public Agencies. In the words of the district court, "under any definition of contract, this is a contract. (cases cited)." (J.S. 30a). The suggestion to the contrary is preposterous.

B. APPELLANTS ARE OBLIGATED UNDER THE CONTRACT TO PERFORM ACCORDING TO ITS TERMS, WHICH INCLUDE THE PUBLIC AGENCIES' RIGHT TO TERMINATE

This Court repeatedly has affirmed the obligation of the United States to meet its contractual commitments. "The United States are as much bound by their contracts as are individuals." *Sinking Fund Cases*, 99 U.S. 700, 718, 719 (1878). "If they repudiate their obligations, it is as much a repudiation, with all the wrong and reproach that term implies, as it would be if the repudiator had been a State or a municipality or a citizen." *Id.* Quoted in *Perry v. United States, supra* at 350, 351. See also *Lynch, supra* at 576, 577. "When the United States, with constitutional authority, makes contracts, it has rights and incurs responsibilities similar to those of individuals who are parties to such instruments." *Perry, supra*, at 352. See also the quotation from Alexander Hamilton, *supra*, at fn. 3 of this Brief.

Notwithstanding these clear statements which never have been repudiated, the Secretary claims that he is not bound by his contractual obligation to honor the Public Agencies' termination notice. The conclusions he advances to support his thesis are varied. Responses to these will appear in the discussion which follows.

1. The Agreement is a contract which is binding upon the United States.

The Secretary argues that Section 418 Agreements merely are a "method of federal regulation" with a "contractual aspect" but that they "cannot be viewed in the

same manner as a bilateral contract governing a discrete transaction." Citing *Bennett v. Kentucky Department of Education* (hereafter *"Kentucky"*), 105 S.Ct. 1544, 1552 (1985). (U.S. Br. 18, 19.) He attempts to force Section 418 Agreements into the mold of the federal grants this Court discussed in *Kentucky* and similar cases. He takes out of context the quoted language from *Kentucky* to support his contention that the Agreement is not a contract. But he fails to point out that that case dealt with a *federal grant program* through which federal funds were administered through the states. That process is an inversion of that of the Social Security System in which the State collects funds from its constituents to be funneled to the federal government. It is clear then that the Secretary's suggestion that Section 418 Agreements are "cooperative federal-state" programs effectuating a "regulatory policy" such as those created and administered under the Food Stamp Act and other similar programs misconceives the nature of such agreements (See U.S. Br. 18 and 19). The only "cooperation" here involved is that the State collects money for the federal government. It acts merely as a conduit. The funds are administered by the United States, which has sole discretion over how and where they are to be spent. This distinction is critical and is fatal to the Secretary's analysis.

In any case, as the ensuing discussion will show, the language in *Kentucky, supra*, when viewed in context with *Bennett v. New Jersey* (hereafter *"New Jersey"*), 105 S.Ct. 1555 (1985) and *Bell v. New Jersey and Pennsylvania* (hereafter *"Bell"*), 461 U.S. 773 (1983) supports the Public Agencies' contentions rather than those of the Secretary. But the common thread in those cases is the question of compliance by States with terms agreed to

by them as a condition of obtaining federal grants. They did *not* deal with the facts before this Court—a written contract executed by the United States.

Independent of written contracts such as the one under discussion, this Court has drawn a clear distinction between statutory *contracts* on the one hand and statutes which set forth *"mere regulatory policy"* on the other. Of first importance is an examination of the statute's language. "If it provides for the execution of a written contract on behalf of the state the case for an obligation binding upon the state is clear." *National R. Passenger, supra* at 15. Inferentially, in such a situation, the *Social Security Act* would be binding independent of the Agreement. Here the Court need not go that far. Not only does Section 418 provide for the execution of a written contract, but a written agreement was in fact executed on behalf of the United States. It is from that written Agreement that the Public Agencies obtain their contractual rights. In that circumstance the case for an obligation binding upon the United States is more than compelling. It is overwhelming.

2. The binding nature of the Contract is not altered by 42 U.S.C. Section 1304, which authorized Congress to amend the enabling statute.

The Secretary contends that 42 U.S.C. Sec. 1304 gives him license to alter or amend the Act even if such alterations and/or amendments result in the repudiation of significant terms of the Agreement. (U.S. Br. 20.) As cogently observed by the district court, "From this language, the defendants appear to argue that there was no contract for them to breach." It has been demonstrated

that there *is* a contract which binds the United States and the Public Agencies. That contract is memorialized in a written Agreement. While the Agreement is authorized by statute it exists independently thereof. "Section 1304 does not authorize the Congress to alter or amend the *contract;* it only authorizes the Congress to alter or amend the *statute.*" (District Court Decision J.S. 30a through 32c.) "The state's right to terminate draws its independent existence from the plain terms of the contract it executed with the United States." *Id.*

In the *Sinking Fund Cases, supra,* this Court considered a similar reservation of power. Mr. Chief Justice Waite held that while under such a reservation of power Congress may retain the power to amend the original charter (in this case the enabling statute), "[i]n so doing it cannot undo what has already been done, and it cannot unmake contracts that have already been made, but it may provide for what shall be done in the future . . . ." *Id.* at 721. The logic behind that statement is compelling. The United States has executed a contract. It cannot now by direct legislation undo its obligation thereunder.

3. The laws which subsist at the time and place of making a contract control its operation.

In a related argument of classic "bootstrap" vintage, the Secretary argues that since the Agreement provides at Section 418(a)(1) that "federal-state agreements may not contain provisions that are 'inconsistent with the provisions of this section'," all that needs to be done to negate the termination provision of the Agreement is to delete that provision from the statute and to substitute a provision which precludes termination. (U.S. Br. 24.)

To contend as does the Secretary that Sections 1304 and 418(a)(1) are "self destruct" clauses giving Congress the right to change contracts as well as statutes is "absurd." That word was used by this Court to describe a similar proposition in *Murray v. Charleston,* 96 U.S. 432 at 445 (1877): "A promise to pay, with a reserved right to deny or change the effect of the promise, is an absurdity." (Cited with approval in *United States Trust Co. v. New Jersey,* 431 U.S. 1, at 24 fn. 22 (1977).)

This Court repeatedly has held that "The laws which subsist at the time and place of the making of a contract" rather than amendments to the laws enacted after the contract's execution, control its interpretation. *Home Building & Loan Assn. v. Blaisdell,* 290 U.S. 398, 429-430 (1934), quoted with approval in *United States Trust, supra,* at 20 and 22. See also *Kentucky, supra* at 105 S.Ct. 1553 (1985) and *New Jersey, supra* at 105 S.Ct. 1556 (1985) " . . . obligations generally should be determined by reference to the law in effect when the grants were made."

That position makes eminent sense. "To say that Congress may withdraw or ignore that pledge is to assume that the Constitution contemplates a vain promise; a pledge having no other sanction than the pleasure and convenience of the pledgor. This Court has given no sanction to such a conception of the obligations of our government." *Perry v. United States, supra* at 351. Quoted with approval in *National RR Passenger, supra,* at 20 fn. 24.

Neither the Public Agencies nor the district court dispute Appellants' contention that it is "black letter law that contracts must be deemed to incorporate the terms

of relevant statutes." (U.S. Br. 25.) The key to that proposition is the word *"relevant."* Only those statutes which "subsist at the time and place of making the contract" are *relevant*. *Amended* Section 418 did *not* subsist at the time the Agreement was negotiated or executed. Nor did it exist for more than a quarter of a century thereafter. Clearly it is not *"relevant"*.

4. To hold that the United States is bound by its contractual obligations does not derogate from its sovereignty.

The Secretary contends that binding the United States to its contractual commitments would impair its "sovereign power."[7] The contention takes several forms which span pages 25 through 42 of U.S. Brief. They evidence a basic misunderstanding of the district court's opinion. The misunderstanding is most clearly articulated at page 32 of said Brief wherein they make the astounding statement that "[i]f the court below meant to hold that Section

---

[7] A similar contention was made in *Perry* v. *United States, supra* at 353 and 354. This Court's reply was as follows:

> *"The argument in favor of the Joint Resolution, as applied to government bonds, is in substance that the government cannot by contract restrict the exercise of a sovereign power. But the right to make binding obligations is a competence attaching to sovereignty.* In the United States, sovereignty resides in the people who act through the organs established by the Constitution. (Cases cited). The Congress as the instrumentality of sovereignty is endowed with certain powers to be exerted on behalf of the people in the manner and with the effect the Constitution ordains. The Congress cannot invoke the sovereign power of the people to override their will as thus declared." (Emphasis added.)

See also, fn. 2 hereof wherein appear the words of Alexander Hamilton quoted with approval in *Perry, supra* at 351 fn. 2.

418 agreements must be construed in a way that would prevent Congress from making essential modifications in the Social Security System," its decision cannot be reconciled with this Court's decisions that "federal and state 'governmental powers cannot be contracted away' ".

There could be no more patent mischaracterization of the district court's holding. That court repeatedly stated that it dealt with abrogation of *contractual* provisions rather than with the power of Congress to make "essential modifications" in the enabling statute.

North American Commercial Co. v. United States, 171 U.S. 110, 137 (1898), cited by the Secretary at U.S. Br. 32 to support his sweeping conclusion that "federal and state 'governmental powers cannot be contracted away' " is inapposite. Unlike the case at bar, the agreement in that case was a "lease" granting an exclusive right to *North American* to hunt seals in a specified location. The "lease" was silent regarding restrictions on numbers of seals to be taken except that it provided that *North American* "agrees to obey and abide by any restrictions or limitations upon the right to kill seals that the Secretary of the Treasury shall judge necessary . . . ." When the Secretary placed a limit on the number of seals to be taken in 1893, *North American* refused to pay its rent, claiming that it had been deprived of the fancied right to take unlimited numbers of seals. There was in fact no such right either written or implied. In fact, the above quoted provision stated precisely the reverse. By contrast, the Agreement in the case at bar contained an express written provision for termination of Social Security by the State or the Public Agencies.

Speaking for this Court Mr. Justice Cardozo asserted that "sovereigns may contract without derogating from their sovereignty." *Steward Machine Co. v. Davis,* 301 U.S. 548, 597 (1937) citing *Perry, supra* at 353. In a different context, but also relevant to the case at bar, this Court said that to require "States to honor the obligations voluntarily assumed as a condition of federal funding . . . simply does not intrude on their sovereignty." *Bell v. New Jersey and Pennsylvania,* 461 U.S. 773, 790 (1983). That case emphasized the free choice exercised by the states pursuant to *statutes. There was no written agreement* as in the case at bar. There were nothing more than statutory conditions which attached to the obtaining of federal funding.

In the case at bar the United States "voluntarily assumed as a condition" of the entry by California and the Public Agencies into the System, their right to terminate the Agreement. The United States "freely gave its assurances that it would abide by the conditions" of its contract. See, *Bell, supra* at 790.

Again it must be emphasized that holding the United States to its bargain cannot be construed to mean that it is "bound never to depart from the terms of the Section 418 *program* as they were established in 1950." (See U.S. Br. 24-25.) (Emphasis supplied) The United States is free, within constitutional restraints, to change the "program" by amending the statute. What it may *not* do is abrogate contractual terms to which it already has agreed in writing.

The Secretary strongly urges that Congress could have swept *everyone* into the System, with the result that

the Agreement would have been rendered nugatory anyway. That being the case, so the argument goes, the *methods* used by Congress should not be questioned. What Appellants really seek is a ruling that "the end justifies the means." In this case the "means" contended for are those which at the moment appeared to be the most *convenient* of the numerous options available to them regardless of ethical and constitutional considerations. There may be societies in which such an approach is acceptable. But it does not fit into our constitutional and ethical system.

Of course that question (whether Congress could have required mandatory universal coverage) is not before the Court. A determination of the constitutionality of such legislation must await the attempt.

The inconsistency of the Secretary's arguments also is elsewhere apparent. On the one hand he argues that binding him to this contract would immobilize future Congresses presumably even from constitutionally defensible changes in the System. Yet he argues also that Congress *could* have changed the System in a manner consistent with the Constitution. He can't have it both ways. In fact Congress is not immobilized. It has latitude to do whatever is lawful and constitutional.

5. Neither convenience nor the lessening of expenditures nor the raising of revenues are valid justifications for the Congress to repudiate its contractual obligations.

The foregoing would appear to be self-evident. Yet the Secretary argues that because Congress found it "most efficacious" to reach its goal by repudiating its contractual obligations it is permissible to do so. The argument

appears to be one of *convenience.* (See, U.S. Br. 32, 33) This Court addressed that issue in *Perry, supra* at 350-351. It concluded that the United States is not free to repudiate its obligations simply because a later Congress finds "their fulfillment inconvenient."

Perry also addressed the question of whether the need to reduce expenditures would justify repudiation of a contractual right. It should be recalled that *Perry* was decided in 1935, at the height of the Great Depression. (*Lynch, supra,* was decided in 1934.) The social and economic environment was so desperate as to make the Social Security "crisis" of 1983 pale into insignificance. Notwithstanding the extremity of that situation, this Court held that the United States is bound by its contractual obligations (at 350 to 354).

In *Lynch,* Mr. Justice Brandeis duly noted the problems created by the Depression. Yet he affirmed that Congress "is without power to reduce expenditures by abrogating contractual obligations of the United States." To do so would be "not the practice of economy, but an act of repudiation . . . ." (at 580). The *raising* of revenues, which was the main reason for the enactment of the 1983 Amendments, also does not justify the abrogation of contractual obligations of the United States by the United States.

The foregoing is consistent with the principle enunciated long ago in the *Sinking Fund Cases, supra,* that the United States "are as much bound by their contracts as are individuals." (99 U.S. at 719) That principle was affirmed by Mr. Justice Brandeis in *Lynch, supra:* "When the United States enters into contract relations, its rights

and duties therein are governed generally by the law applicable to contracts between private individuals." (292 U.S. at 579) Accord, *Perry, supra* at 352 and *S.R.A. Inc. v. Minnesota,* 327 U.S. 558, 564 (1946). (For a cogent analysis of the application of federal common law of contracts to the case at bar please see *Amici Br.* Arguments I and II.)

It is clear that had the termination provision under discussion been between individuals no principle of contract law would have justified the unilateral repudiation thereof by one of them. Yet the Secretary contends that because the United States is a sovereign the principles governing contracts do not apply. It has been demonstrated that "sovereigns may contract without derogating from their sovereignty." *Steward Machine Co., supra* at 597.

The Secretary attempts to avoid the holdings of *Perry* and *Lynch* by arguing that the facts in those cases dealt with an entry by the state into "financial and other markets." (U.S. Br. 36 citing *Energy Reserves Group, Inc. v. Kansas Power & Light Co.,* 459 U.S. 400, 412-413 n. 14 (1983) and *United States Trust Co. v. New Jersey, supra* at 25 (1976).) The implication is that these cases hold that *only* where the United States enters "financial and other markets" is it bound by its contractual obligations. This Court never has so held.

But even were one to assume *arguendo* that entry by the United States into "financial and other markets," and "investment-backed expectations" (U.S. Br. 18) are prerequisites to binding the United States to its contractual obligations, the Secretary could not prevail. A primary

reason for the exodus of increasing numbers of Section 418 employees from the System was that coverage could be provided elsewhere less expensively. (See, Dist. Ct. Docket Entry 10 at page 3). The System is competing in the marketplace not only with State pension plans but also with private enterprise. It is no secret that the insurance "market" is very large and that the competition is keen. That it qualifies as a "financial or other market" is beyond reasonable dispute.

Further, the State and the Public Agenies do in fact have "investment-backed expectations" of substantial proportions in their own pension programs. The PERS of California is one example. As costs of government increase and available financial resources decline, the burden of paying for two pension programs already has become intolerable for Public Agencies.

It must be emphasized that the Public Agencies submit the foregoing analysis regarding "business purposes" and "markets" and "investment" *arguendo* only. They do ***not*** thereby in the least concede that only in those circumstances may the United States be held to its bargain.

It is asserted also that *Lynch, supra,* stands ***only*** for the proposition that "need for money is no excuse for repudiating contractual obligations." (U.S. Br. 37) (Emphasis added). That that conclusion is not factual is demonstrable.

While the quoted words, which are taken from *United States Trust, supra* at 26 n. 25, arguably express the narrowest possible "holding" of that case, *Lynch* "stands for" much more.

For example, in *Lynch,* this Court expressly rejected the notion embodied in the aforementioned argument that contracts "not entered into by the United States for a business purpose" were entitled to be treated differently than those which are. To the contrary, the Court said: "[b]ut the [war risk] policies, although not entered into for gain, are legal obligations of the same dignity as other contracts of the United States and possess the same legal incidents." (*Lynch, supra* at 576). That principle has direct application to the case at bar.

Lynch was concerned with insurance in the form of War Risk Insurance policies which were held to constitute contracts obligating the United States. "As consideration for the government's obligation, the insured paid prescribed monthly premiums." *Lynch, supra* at 576. Here also we are concerned with insurance. The Secretary calls it the "Nation's basic social insurance program." (U.S. Br. 17). The insureds pay a prescribed premium to their employers, also "as consideration for the government's obligation." The basis for their involvement is the agreements which have been discussed. As in *Lynch,* the terms of these agreements are contractual obligations. That includes the obligation of the United States to allow the Public Agencies to terminate their coverage under the Act.

In *Lynch* Congress had sought to relieve the financial burdens of the Depression by renouncing its obligations under the War Risk policies. In this case it sought to relieve the financial concerns of the Social Security System by among other measures renouncing its contractual obligations with the State and the Public Agencies.

Notwithstanding the Secretary's protests that there were other "concerns," the overwhelming reason for pas-

sage of the 1983 Amendments, which included the repudiation of the termination option, was the perception of a financial crisis. Hence the title by which it commonly was known, the Social Security "Rescue" Bill. Even under the narrowest holding of *Lynch, supra,* the repudiation of the termination option was improper. And yet the "crisis" facing the System in 1983 was minor when compared to the overwhelming financial challenges of the Great Depression during which *Lynch* and *Perry* were decided.

6. In revoking the termination option Appellants have breached a substantial provision of their contract with the Public Agencies.

The Secretary does not dispute that the Public Agencies complied with the prerequisites for termination. That they did so is clear from the district court record. (See, e.g., Docket Entry 10, Baker, *supra,* together with Exhibit B thereto consisting of seven pages incorporating a letter and other documents from the City of Arcata.) All of the prerequisites were filled. The district court so found.

It has been shown that the termination option was a substantial factor in enticing the Public Agenies to enter the System. (See, *Statement, supra,* and Declarations of Richard Ramirez, J.A. 64 through 67 and Richard T. Baker, cited therein.) The obvious reason for the "escape clause" was that it might someday need to be used. Its need would be dictated by the exigencies of the times. "The City of Lincoln entered the Social Security program with the understanding and assurance that if the circumstances suggested it, the City would be able to terminate . . . ." (J.A. 72 par. 13). One of those "circumstances" actually occurred: a lack of sufficient funds to

keep employees in two or more retirement systems and still perform essential services. (J.A. 64 through 73).

It is anomalous indeed that the occurrence of the very contingency the "escape clause" was intended to protect the Public Agencies against, has been used as a sword to separate them from their bargained for shield.

The fact is that the System is substantially more expensive today than it was when the Public Agencies became involved. And it promises to become even more so. It is this rapid escalation of costs to support the System which has motivated them to seek more competitive ways of providing coverage for their employees. For many local governments the choice is between that and financial disaster. The termination option was calculated to save them from such a fate. Clearly it was a substantial enticement to enter the System.

Far from irresponsibly depriving their employees of insurance coverage as the Secretary suggests, many if not most California local government entities have carried double coverage. (See, e.g., J.A. 72—Ramirez, par. 15). In making the choice to terminate Social Security they have deliberated extensively and consulted with their affected employees. The choice to terminate was made as the option which best would serve both their employees and their constituency.

From the foregoing it is clear that the United States entered into a contractual relationship with the Public Agencies and that it breached a substantial provision of that contract to the Public Agencies' detriment. That alone should suffice to affirm the district court's judgment.

II

THE REPUDIATION OF THE TERMINATION OPTION BY THE UNITED STATES CONSTITUTED A TAKING OF PROPERTY WITHOUT JUST COMPENSATION WITHIN THE MEANING OF THE FIFTH AMENDMENT

The Just Compensation Clause provides that "private property" may not be taken for a public purpose without just compensation. (U.S. Constitution Amendment 5). The district court held that a "California *public* agency (a political subdivision of the State) may possess 'private property' within the meaning of the Just Compensation Clause." Citing *United States v. 50 Acres,* 105 S.Ct. 451, 456 (1984). (J.S. 16a and 17a).

It is clear that the Public Agencies are "persons" within the meaning of the Fifth and Fourteenth Amendments. *Township of River Vale v. Town of Orangetown,* 403 F 2d 684 at 686 (2nd Cir. 1968); *City of Boston v. Massachusetts Port Authority,* 444 F 2d 167 at 168 (1st Cir. 1971); *Owen v. City of Independence, Mo.,* 445 U.S. 622 at 639, 100 S.Ct. 1398 at 1409 (1980); see also, *Monell v. New York City Dept. of Social Services,* 436 U.S. 658 at 687 (1978); *City of Santa Clara, Cal. v. Andrus,* 572 F 2d 660 at 675 (9th Cir. 1978); *Housing Authority of City of Asbury Park v. Richardson,* 346 F. Supp. 1027 at 1032 (1972).

Because they are "persons" they may assert constitutional claims. The district court so held.

The district court held also that "[A]s a general rule, rights which arise out of contracts with the United States are 'property' within the meaning of the Fifth Amendment." (J.S. 19a). In so holding it quoted from *Lynch, supra* at 579 as follows:

> "The Fifth Amendment commands that property be not taken without making just compensation. Valid contracts are property, whether the obligor be a private individual, a municipality, a State or the United States. *Rights against the United States arising out of a contract with it are protected by the Fifth Amendment.*" (Emphasis added).

(See also, *United States v. Petty Motor Company,* 327 U.S. 372, 374 (1945); *Armstrong v. United States,* 364 U.S. 40, 42-46 (1960)).

The Public Agencies have "rights against the United States arising out of a contract with it" either on their own account or as third-party beneficiaries. By its own terms the federal-state Agreement was to "*include* political subdivisions or coverage groups" which were added through "modifications" to the Agreement. (J.A. 31 par. (E) Modification). They thereby became a part of the Agreement and have the right to enforce its terms on their own account.

Even if it were assumed that the Public Agencies do not have such rights on their own account, they do have them as third-party beneficiaries. That the Agreement entered into was for their benefit is beyond dispute. (See district court analysis on this issue at J.S. 20a through 22a. See also, *Regulations to Section 218 of the Act,* Section 404.1201 General effect of Section 218 of the Act: State and Federal Governments to enter into Agreement "for the purpose of extending to certain employees of the State and its political subdivisions protection accorded other employees. . . ." (Title 20 CFR Sec. 404.1201(a)). Accordingly, the Public Agencies have rights arising out of the contract with the United States.

While the Secretary seems to concede that the contract was "impaired," he argues that this impairment is not of "constitutional dimension," that the "destruction of one strand of the bundle" of property rights is not a taking. (U.S. Br. 42.) He argues further that the "economic impact" of the repudiation of his contractual obligation is minimal and that to affirm the district court "would permit persons to 'remove their transactions from the reach of dominant constitutional power by making contracts about them.' " (U.S. Br. 43).

In advancing those arguments the Secretary ignores the central facts of this case: that the "dominant constitutional power" to which the Secretary refers is *Congress;* that *Congress* enacted the legislation which authorized the United States to execute the Agreement containing a termination option; and that *pursuant to said Congressional authority the United States executed the Agreement and is one of its parties thereto.* That legislation with its resulting Agreement was the mechanism through which *Congress* adjusted "the benefits and burdens of economic life." It must be emphasized that *none* of the cases cited by the Secretary to support his arguments on these issues deal with facts such as those of this case.

The "bundle" of property rights in dispute is not the Agreement as a whole. Rather, the termination option is the *entire* "bundle". And it has been repudiated by Congress in its entirety. It was not modified. It was abrogated. There are no "strands" left. The argument that Appellees have lost only one "strand" of their "bundle" of rights because they still have the rest of an Agreement which they want to terminate is absurd. The destruction

of the right to terminate of necessity effectively destroyed the value to the Public Agencies of the entire agreement.[8]

Some "values" inherent in the termination option already have been discussed. It should not be overlooked that the economic impact on the states and public agencies of repudiation of that option is very substantial. As cogently pointed out in *Amici Br.* Argument, par. II, "California—and other contracting States—must under the 1983 Amendments continue to pay large sums of money for coverage of employees of political subdivisions which no longer desire such coverage. . . . By any measure, such an effect is hardly *de minimus.*" Far from being *de minimus,*

---

[8] In the closing paragraphs of his Brief (See, U.S. Br. 43 through 45) the Secretary advances several arguments of such marginal if any relevance that they require no comment except to acknowledge that they exist. A typical example is his suggestion that "any expectation on the part of appellees that they would never be required to participate in Social Security against their will cannot be deemed reasonable." Citing *Ruckelshaus v. Monsanto Co.*, No. 83-196 (June 26, 1984) slip op. 17 and *Webb's Fabulous Pharmacies, Inc. v. Beckwith,* 449 U.S. 155, 161 (1980).

The portion of the cited cases referred to is the restatement of the principle that "a mere unilateral expectation or an abstract need is not a property interest entitled to protection." *Webb, supra,* at 161. As with so many of the Secretary's arguments, the suggestion sets up a straw man. There has been no discussion on the part of anyone of any expectation that Social Security never would become mandatory, although such an expectation at the time the agreements were executed clearly would have been reasonable. That question is not at issue. Its insertion confuses rather than illuminates. The question in this case deals with a contractual obligation of the United States freely negotiated and entered into. Surely the inclusion of that provision in the contract raised a *bilateral* understanding if not an expectation that the option to terminate someday might be exercised. It therefore is obvious that the principle for which the Secretary cites *Monsanto, supra* and *Webb, supra* does not apply to the facts of this case. A similar conclusion applies to all of these marginal arguments advanced by the Secretary.

the financial impact on the Public Agencies independent of that on the State is in some cases devastating. (See, J.A. 64 through 73 and District Court Docket Entry 7 and 10, Baker Affidavits). And the impact on the State and its political subdivisions in the aggregate is enormous. Clearly, valuable contract rights belonging to the Public Agencies have been expunged by the 1983 Amendments.

III

IN SCRUTINIZING THE GOVERNMENT'S REPUDIATION OF ITS OWN CONTRACTS FOR APPLICATION OF THE JUST COMPENSATION CLAUSE, "A HEIGHTENED STANDARD OF REVIEW" SHOULD APPLY

The "standard" of review proposed by the Secretary is in fact a non-standard calculated to give the United States license to abrogate contractual commitments at will. This Court has observed that there is a "clear distinction between the power of Congress to control" or interdict the contracts of private parties when they interfere with the exercise of constitutional authority, and the power of Congress to alter or repudiate the substance of its own engagements. . . ." *Perry, supra,* 350-351, cited in *National RR Passenger, supra,* 20 n. 24. In *National RR Passenger, supra,* the Court suggested that in cases such as this, a "heightened standard of review" apply.

"An appropriate standard," suggest *Amici* in their Brief, "is found in *United States Trust Co.*" (*Amici Br.*, Argument III). *United States Trust Co., supra,* was decided in the context of a *state's* breach of its contractual obligations. Public Agencies submit that the federal government should be required to pass a test at least as stringent as the one there set forth. This Court there held

that it could sustain the State's repudiation of its contractual obligations only if the "impairment was both *reasonable and necessary* to serve the admittedly important purposes claimed by the State." *Ibid.* at 29. (Emphasis added). It concluded that the burden is on the government to show that "an evident and more moderate course would [not] serve it's purposes equally well." (*Id.* at 31).[9]

Under either prong the 1983 Amendments must fail. The Secretary contends that "Congress plainly acted rationally in distinguishing between state and local government employees who currently are participants in the System and those who do not. Expanding coverage to workers outside Social Security would mean displacing existing pension systems . . . and would impose double burdens on states or localities that currently operate 'pay as-you-go pension plans. . . .' " The speciousness of that argument is apparent from the fact that the 1983 Amendments swept into the System employees of all nonprofit organizations without regard to whether some of them had existing plans in place.

---

[9] In a brief concurring opinion Mr. Chief Justice Burger stated his understanding of the holding as follows:

> " . . . the State must demonstrate that the impairment was essential to the achievement of an important state purpose. Furthermore, the State must show that it *did not know and could not have known the impact* of the contract on that state interest at the time the contract was made." (*Id.* at 32). (Emphasis added).

Clearly the United States knew or could have known at the time the contract was executed that Public Agencies would exercise their option to terminate in the appropriate circumstances. They further knew or could have known that the exercise of that option by Public Agencies and others would diminish contributions to the System and might ultimately become a cause for financial concern.

That there were other available options short of the drastic one of repudiating contractual obligations is clear. For example, with regard to *federal* employees, only ***new*** employees were required to join the System. (Pub. L. No. 98-21, Sec. 191, 97 Stat. 67.) Yet *all* nonprofit employees were required to enroll. (*Id.*, Sec. 102(a) (1), 97 Stat. 70.) And the Secretary contends that Congress *could* have included all State and Local employees. He suggests that it pursued the challenged course because it was "most efficacious" and describe it as a mere "semantic defect" which has no "independent constitutional significance." (U.S. Br. 32). None of those euphemisms qualify the repudiation of the termination provision as "reasonable and necessary." To the contrary, they are a clear admission that the repudiation was neither reasonable nor necessary.

The foregoing options are only some of those that could have been adopted. It is obvious that it was not necessary for the Congress to repudiate its contractual obligations. As was incisively observed in the *Amici Br.*, Argument III:

> "The fact that Congress could have reached the same end through permissible means hardly serves, as the Secretary suggests, to render 'absurd' the argument that the Government's repudiation of its contracts is constitutionally impermissible. (U.S. Br. at 13.) The Fifth Amendment—as much of the Constitution—is largely about *process*, not results. It is permissible to deprive a person of life, liberty or property, the Constitution teaches, only after due process of law. Just as it is no answer to a valid Fifth Amendment claim in the criminal context to say that a fair trial would surely have produced the same result, it is no answer in this case for the Secretary to contend that a different legislative approach might constitutionally lead to the same practical result. Indeed, since it is plain

> that it was not necessary for Congress to repudiate the 1951 Agreement in order to avoid financial loss to the System, its decision nonetheless to abrogate its agreements with the States is wholly indefensible."

CONCLUSION

This Court repeatedly has asserted that *States* are bound to honor their contractual obligations to the United States. See, e.g., *Bell, supra;* and *Pennhurst State Hospital v. Halderman,* 451 U.S. 1 at 17 (1981). That the United States in turn is bound to honor its contractual commitments to the State and the Public Agencies is central to our federal system and is consistent with principles of justice and fairness. If the United States may abrogate its solemn promises made to the State and the Public Agencies in a written agreement, then "federalism" indeed is an empty word. Further, the legitimate expectations of parties to contracts would go unfulfilled.

A contract contemplates mutual benefits and obligations. The very concept of contract belies the notion that one of the parties, even if it perceives itself as being more powerful than the other, unilaterally may change the contract's terms. Here two sovereign entities have by written contract made pledges to each other. In reliance on these pledges one of these sovereigns has made similar pledges to yet other parties which are an integral part of our federal system. The other sovereign (United States) expressly and in writing has extended its pledges to encompass those other parties. And those other parties also made commitments in reliance on the pledges of the United States.

But more than federalism and the sanctity of contract are at stake. If the government of the United States is free at its convenience to ignore its solemn contractual commitments the erosion of confidence of average Americans in their government surely will be immense. Particularly is this true where, as seems to have been the case with the 1983 Amendments, the elected representatives of the people are not free to work their will on the legislation before its enactment.[10]

---

[10] There is evidence that the process by which the 1983 Amendments became law itself was flawed and may well have circumvented the political safeguards of federalism contemplated by the Constitution. Among the factors which lend support to that conclusion are the following excerpts from statements made by two Congressmen who protested the "gag rule" which the House leadership had imposed upon them.

Congressman Gonzalez explained that he could not support a bill "that is drawn up in a matter of days, when we know that the recommendations behind it were arrived at after months of struggle, and then only after the Commission was force-fed. The issues . . . are immense. They deserve more careful consideration than we are permitted to give today . . ."

And Congressman Addabbo noted that the Social Security bill "may be the most critical piece of legislation to come before this Congress this session . . . This entire charade has been a political blitzkrieg in which those of us who have raised questions about the validity of what we are doing and the extent of harm we are causing innocent people have been brushed aside in the rush to bring this bill to the floor before reason can assert itself." (See, Cong. Record, House, March 9, 1983, H 951, 1004-1005).

The highly unusual process through which the Bill became law would seem to dictate that less deference than usual be paid to this legislative enactment and greater than ordinary scrutiny be exercised by the Court.

Honoring of pledges builds reliance and trust and stability in relationships among individuals and sovereigns. That trust is the oil which keeps the machinery that is society running if not always smoothly, at least running.

The repudiation of pledges, on the other hand, leads inexorably to frustration and distrust and instability. With the oil gone the resulting friction can lead only to a breakdown of the machinery. The Secretary has given no valid reason why he should be given license to abandon his pledges. The people of the United States and the several states would be ill served were he allowed to do so.

The judgment of the district court should be affirmed.

Respectfully submitted,

ERNEST F. SCHULZKE

Attorney for Appellees
Public Agencies Opposed to
Social Security Entrapment, et al.

March 1986